No. 94-755

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

WILLIAM CHANOFF, DAVID CHANOFF, RACHEL CHANOFF and HARRIET FINGEROTE,

Petitioners,

—v.—

UNITED STATES SURGICAL CORPORATION, LEON HIRSCH, TURI JOSEFSEN, BRUCE C. LUSTMAN and MARIANNE SCIPIONE,

Respondents.

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Should this Court grant *certiorari* to decide petitioners' first question, concerning whether their six state law claims were preempted by the anti-tippee norms of the federal securities laws, when both courts below also rested dismissal of each claim independently on one or more state law grounds?

2. Should this Court grant *certiorari* to decide the second question, challenging the state law holding (affirmed by both courts below) that the damages sought on the six state law claims are too speculative under Connecticut law, in view of the policy against this Court's review of state law claims and the fact that dismissal of those claims also rests on multiple independent and adequate state law grounds, including that the damages sought were not proximately caused by the wrong of which petitioners complain?

3. Should this Court grant *certiorari* to decide petitioners' third question, concerning whether the purchaser-seller rule of *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), applies to civil RICO cases, when the dismissal of petitioners' RICO claims also rests on multiple independent grounds, including that petitioners, who neither bought nor sold securities during the period of the alleged wrong, (a) did not allege any injury that could be found proximately related to the alleged wrong as required by *Holmes v. Securities Investors Protection Corp.*, 112 S. Ct. 1311 (1992), (b) did not allege any non-speculative injury, (c) did not allege any facts constituting "fraud in the sale of securities" as required by 18 U.S.C. §1964(c), and (d) did not allege any cognizable injury to their property under the federal wire and mail fraud statutes?

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COUNTER-STATEMENT OF THE CASE

The case petitioners describe bears only a fleeting and fractured resemblance to the case presented in petitioners' complaint and argued to the district court. For present purposes, however, beyond noting that the "facts" petitioners recite are simply the untested allegations of their complaint assumed to be true under the familiar standard on a motion to dismiss pursuant to Rule 12(b)(6), Fed. R. Civ. P., it should suffice to supplement petitioners' statement of the case with three additional points.

At the heart of their complaint was the basic theory that "a unique relationship of truth and confidence existed between William Chanoff and defendants" (Cmplt. ¶ 116).[1] Thus, petitioners asserted that United States Surgical Corporation ("USSC") and the individual defendants (collectively, "respondents" or "defendants") knew that the information allegedly not disclosed was "of particular concern" to Chanoff (*id.*), that defendants had unique fiduciary duties "to speak fully . . . with William Chanoff concerning USSC" (¶ 121), and that defendants "suppressed and concealed" information from Chanoff personally in order to induce him and his family specifically to refrain "from selling or hedging any of their USSC stock" (¶ 117-18).[2] Petitioners' case was founded on

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[1] "Cmplt. ¶ _" refers to paragraphs of petitioners' complaint, reproduced in Appendix E of the petition for a writ of certiorari ("Pet."). "App. Br. _" refers to pages of Petitioners' brief in the Court of Appeals, and "A_" refers to pages of the Joint Appendix in that court.

[2] Among the allegations whose sole function was to support the claim that Chanoff was entitled to information on the telephone or in writing beyond what had been publicly disclosed were ¶¶ 1, 19, 46, 56, 66, 78-79, 100, 111, 116, 121. Those paragraphs allege the reasons why Chanoff was entitled to information not disclosed

(continued...)

the proposition that William Chanoff and his family were entitled to non-public information from USSC and its Vice President for Corporate Communications, Marianne Scipione, by virtue of his prior position as a director of USSC and continued effort to obtain unique information about the company. Thus, all petitioners' damage allegations presuppose that they would have sold upon receiving information in advance of any other shareholders. *E.g.*, ¶¶ 96(a), 97(a), 98(a), and 99(a).[3]

Further, although petitioners did allege that Chanoff was "asked" by "a stockbroker" to "consider" selling some or all of his stock (Cmplt. ¶ 84), they did not allege that Chanoff (or any other plaintiff) ever asked for Scipione's opinion or guidance as to whether or not he should sell or hedge his USSC holdings; ever informed Scipione that he or she was actually considering selling or hedging, or that his or her decision whether to do so would be based on information that Scipione provided; ever told Scipione that others (including petitioners here) were depending on Scipione's advice; or ever told Scipione that he or she believed he or she had a sufficient

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[2](...continued)
to the public, including that he was constantly fishing for inside information from "defendant Scipione, both by letter and by telephone, concerning various matters affecting the prospects of USSC and the value of its stock." Cmplt. ¶¶ 17-19. At oral argument, plaintiffs' counsel said, "I don't deny that those [the individual conversations that Chanoff had with Scipione] play an important role in our case. They do." A242.

[3] Petitioners do allege the proceeds that a hypothetical sale on January 15, 1992, at the height of the market for USSC stock, would have produced (*e.g.*, ¶¶ 96(a), 97(a), 98(a), and 99(a)), but carefully avoid alleging that they would have sold on that date at the height of the market had the company disclosed to them or to the public the allegedly undisclosed additional information it had as of that time.

relationship with Scipione or with USSC to be entitled to receive material nonpublic information denied to other investors. Cmplt. ¶¶ 46, 66-67, 74, 77-80, 84, 88.

Finally, petitioners alleged no facts concerning the dates on which they would have sold or hedged some or all of their shares had they known "the truth" earlier, much less the number of shares that each petitioner would have sold and/or hedged on particular dates during that sixteen-month period during which USSC's share price steadily dropped. Instead, each petitioner alleged only, to use the representative allegation of William Chanoff, that he or she "declined to sell or hedge any of his USSC stock, as he would have done had he known the truth, from January 1, 1992 until April 9, 1993." Cmplt. ¶¶ 96(a), 97(a), 98(a), and 99(a).[4]

REASONS FOR DENYING THE PETITION

The petition should be denied because the case does not fairly present any of the questions petitioners attempt to raise and does not warrant this Court's review.

Any answer this Court would give to petitioners' first question, concerning whether federal preemption principles barred their six state law claims, would be dicta. Each of those state law claims was also dismissed for one or more independent and adequate reasons under state law.

The second issue presented — concerning whether the damages sought by securities holders for alleged fraud, negligent misrepresentation, breach of fiduciary duty, or violation of a Connecticut securities anti-fraud statute, during a period when those holders neither bought nor sold securities, are unduly speculative — presents a question of

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[4] *See* n. 3 *supra*. Moreover, as the district court observed, "the plaintiffs conceded at oral argument [that] there is not one precise point at which the defendants' duty to disclose information attached . . . . " Pet. C-10.

Connecticut law. This Court does not deploy its discretionary jurisdiction to correct applications of state law. Doing so would be particularly unwise here, where the six state law claims were dismissed not only for unduly speculative damages but also, independently and adequately, on multiple additional state law grounds.

Although there is a federal issue lurking in the third question presented — concerning whether the rule announced in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), applies generally to RICO claims predicated on securities fraud — that question is not properly presented here and any answer provided would be dicta. As both courts below correctly held, the RICO claims pressed here were subject to dismissal under non-*Blue Chip Stamps* grounds, including the proximate cause ground relied on by this Court in *Holmes v. Securities Investors Protection Corp.*, 112 S. Ct. 1311 (1992). Review of those issues has not been sought and cannot be justified under the factors governing this Court's exercise of its discretionary jurisdiction, and in any event each of the grounds relied on for dismissal was plainly correct under long-settled law.[5]

I. PREEMPTION IS NOT PROPERLY AT ISSUE AND WAS CORRECTLY DECIDED

The district court held that the Chanoffs' six state law claims were preempted only to the extent that those claims

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[5] In their argument (although not in the Questions Presented), petitioners contend (at 9-25) that the courts below imposed the *Blue Chip Stamps* "standing" requirement on state law securities claims as a matter of federal law. That contention is wrong; the district court did not so much as mention *Blue Chip Stamps* in the portions of the decision dismissing the state law claims, and cited it for the first time only in the last section, addressing the federal claims. Pet. C-20.

rested on an alleged duty by USSC's Vice President for Corporate Communications "to disclose [nonpublic information] to William Chanoff during their personal exchanges." Pet. C-5-8. The court proceeded, however, to dismiss the state law claims in their entirety on multiple additional state law grounds:

- All six claims were dismissed because "plaintiffs, with limited exception, have not alleged cognizable injury or damage that could be construed as directly or proximately caused by the alleged misconduct as required to sustain the common law causes of action." Pet. C-8.[6]
- As an additional ground for dismissing the breach of fiduciary duty claim, the courts below held that, under state law, "plaintiffs lack standing to assert this claim because defendants owe no independent fiduciary duty to the plaintiffs. . . . . " Pet. C-13.
- The two negligence claims were dismissed "not only for failure to allege proximate injury but also for lack of standing." Connecticut law does not afford a remedy for negligent misstatement or omission to an indeterminate class in an indeterminate amount for an indeterminate time. Pet. C-17-18.
- As an additional ground for dismissing the statutory state law securities claim, the courts held that the statute provided no private right of action. Pet. C-18-19.

Under these circumstances, anything this Court would say about preemption would be dicta.

In any event, both courts below correctly concluded that "to the extent that plaintiffs' state law claims are based on

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[6] The "exception" refers to the claim of William Chanoff concerning a purchase of 2,000 shares, which has been voluntarily dismissed from this action and is not before this Court. *See* Pet. 8 n. 7.

defendant Scipione's failure to disclose certain information to Chanoff during their personal exchanges, these claims are preempted by the federal securities laws which proscribe such selective disclosure." Pet. C-5-6; *see also Basic, Inc. v. Levinson*, 485 U.S. 224, 242 (1988); *Dirks v. SEC*, 463 U.S. 646, 659-60 (1983); and *Chiarella v. United States*, 445 U.S. 222, 228 (1980).[7]

II. THE STATE LAW SPECULATIVE DAMAGE ISSUE DOES NOT WARRANT REVIEW AND WAS CORRECTLY DECIDED

The holding of both courts below that under Connecticut law the damages sought on all six state law claims were too speculative to be litigated (Pet. C-8-19) does not merit review. This Court does not use its *certiorari* jurisdiction to review determinations of state law, especially when both the district court and court of appeals agreed in such a determination. *Haring v. Prosise*, 462 U.S. 306, 314 n. 8 (1983); *Brockett v. Spokane Arcades, Inc.*, 472 U.S. 491, 499-500 (1985); *Butner v. United States*, 440 U.S. 48, 57-58 (1979); Robert L. Stern et al., *Supreme Court Practice* 183 (7th ed. 1993).

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[7] *See also Elkind v. Liggett & Myers, Inc.*, 635 F.2d 156, 165, 169 (2d Cir. 1980) (the "duty imposed on a company and its officers is an alternative one: they must disclose material inside information either to no outsiders or to all outsiders"); *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2d Cir. 1968) (en banc), *cert. denied*, 394 U.S. 976 (1969) ("The only regulatory objective is that access to material information be enjoyed equally"); and *In re Cady, Roberts & Co.*, 40 S.E.C. 907, 1961 WL 3743, at *6 (Nov. 8, 1961) (trading on information obtained in advance of the rest of the market is forbidden "until the established procedures for public release of the information are carried out . . .").

Even if the ruling that the damages sought are unobtainable under Connecticut law were a proper subject for this Court's review, *certiorari* should still be denied, as the dismissal of the six state law claims rested as well on the independent proximate cause and other grounds identified above (at page 5) on which petitioners have not sought review.

The holding precluding the damages sought as impermissibly speculative was in any event so evidently correct as not to warrant this Court's review. Under Connecticut law, "a plaintiff cannot recover profits which might have been realized if he had not been deceived, unless there is evidence by which such profits can be estimated with reasonable certainty." Pet. C-9-10 (relying on *Morrell v. Wiley*, 178 A. 121, 123 (Conn. 1935), and *Pacelli Bros. Transp., Inc. v. Pacelli*, 456 A.2d 325 (Conn. 1983)).

Petitioners' complaint sought as damages the difference between the "unmanipulated" market price at which "the Chanoffs *could have sold their USSC shares* - had respondents promptly and publicly disclosed truthful information . . . and the approximately $30 per share with which they were left, in April, 1993, after defendants belatedly told the truth." (Pet. 21, emphasis added).

These damages are doubly speculative. First, as petitioners' use of the phrase "could have sold" (instead of "*would* have sold") betrays, it is uncertain — and ascertainable at best only by uncorroboratable oral testimony — whether petitioners were damaged at all. (Petitioners, by their own premises, acquired their shares before any alleged fraud-induced price increase; if they would have retained those shares past the time that the price dropped in response

to market disclosure, then they did not lose anything to which they were entitled.)[8]

Second, even on the dubious assumption that the Chanoffs lost something (other than the opportunity to profit from a price their own complaint alleges was unlawful), their alleged market losses are speculative on at least six levels. Petitioners did not allege *any* of the fixed points necessary for a damage calculation: (i) the date on which defendants should have made the allegedly omitted disclosures; (ii) the date(s) (if any) on which plaintiffs would have changed their previously steadfast policy of holding their USSC stock, which they notably maintained for well over a year despite a steadily dropping price, and sold and/or hedged their holdings; (iii) the "unmanipulated" market price of their USSC holdings on the date or dates they would have sold or hedged, which by petitioners' own premises would have involved speculation regarding the actions that would have been taken by thousands of other holders of USSC stock; (iv) the number of shares (if any) they would have sold on that date or those dates; (v) the number of shares (if any) they would have hedged on that date or those dates; and (vi) the extent to which the decline in USSC's stock price, from when they would have sold until April 7, 1993, was attributable to factors other than the alleged fraud.[9]

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[8] *See Crocker v. Federal Deposit Ins. Corp.*, 826 F.2d 347 (5th Cir. 1987), *cert. denied*, 485 U.S. 905 (1988) (plaintiffs who purchase at unmanipulated price are not entitled to profit from the price to which shares are subsequently manipulated by fraud).

[9] Petitioners conceded that they would have to prove that "they would have sold their USSC stock on the open market upon learning of the JIT program" to be entitled to damages. App. Br. 28. Any attempt to do so would have been problematic, in light of the rather different allegation that Chanoff would have sold *or* (continued...)

In the ordinary 10b-5 case, such as those on which petitioners rely (Pet. 22), the dates and sizes of purchases or sales of not only the plaintiffs but also all investors in the issuer's stock are fixed, and all that needs be reconstructed is an unmanipulated share price on the date of trade. *See, e.g., Minpeco, S.A. v. Conticommodity Servs., Inc.*, 676 F. Supp. 486, 495 (S.D.N.Y. 1987); *Sirota v. Solitron Devices, Inc.*, 673 F.2d 566, 576-78 (2d Cir.), *cert. denied*, 459 U.S. 838 (1982). The case-authorized damage models for such circumstances do not require speculation about what investors in the issuer's stock who did not buy or sell during the damage period would have in fact done if the alleged undisclosed information had been available to all the issuer's stockholders.

By contrast, the problem posed by petitioners' holder claims is not merely the limited uncertainty of ordinary 10b-5 cases, requiring only the reconstruction by expert testimony of an "unmanipulated" value on a fixed date, but a far more impenetrable thicket of speculation and doubt. Most importantly, it is wholly speculative whether, when, and how

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[9](...continued)

hedged all, *or some*, of his stock (Cmplt. ¶¶ 84, 96(a)), and counsel's concession at oral argument in the district court that Chanoff "never had any intention of selling his U.S. Surgical stock." A260; *see also* A254 ("we do contend that our clients would have *been able* to sell their stock or at least to hedge it at a price which reflected the market's evaluation and analysis . . .") (emphasis added). These vague and conflicting formulations directly implicate the concerns expressed in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), strongly reaffirmed in *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083 (1991), about the integrity of the judicial process and the hydraulic pressures that holder claims would impose on plaintiffs to provide false oral testimony in circumstances where no corroboration is likely to be available.

many shares petitioners would have sold or hedged; and it is equally speculative whether, when, and how all the thousands of other holders of USSC shares would have sold or hedged. Based on the answers provided to those key questions, experts would have had to reconstruct prices for each such date of selling or hedging, as well as determine what part of the subsequent steady drop to April 7 was attributable to the alleged fraud.

As both courts below saw, these additional undeterminable factors (which the petition ignores) place resolution of petitioners' unpreempted state law claims in the domain of dart-throwing or fortune-telling, and well outside the domain established by Connecticut for the reasonable ascertainment of damages under law. Permitting a jury to award damages in such a case would offend every policy underlying the traditional judicial refusal to allow lost profits except where they can be estimated with reasonable certainty.[10]

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[10] Permitting jury awards in those circumstances would also offend the policies relied on by eight members of this Court in *Virginia Bankshares*, policies of such compelling nature that there is no reason to doubt that they would move most state courts as well. As Justice Souter wrote for the Court (501 U.S. at 1092),

> Recognizing liability to merely would-be investors [or sellers], however, would have exposed the courts to litigation unconstrained by any [] anchor in demonstrable fact, resting instead on a plaintiff's "subjective hypothesis" about the number of shares he would have sold . . . . Hindsight's natural temptation to hypothesize boldness would have magnified the risk of nuisance litigation, which would have been compounded both by the opportunity to prolong discovery, and by the capacity of claims resting on undocumented personal assertion to resist any resolution short of settlement or trial. Such were the premises of policy . . . on which Blue Chip Stamps deflected the threat of

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Petitioners attempted to eliminate some of this uncertainty by telling the Second Circuit that they would have done better than other investors if the requisite information had been given to both William Chanoff and the public generally. App. Br. 17-18. By their own hypothesis, however, the price would have dropped upon public disclosure to its "unmanipulated" level (wringing out of the stock price the claimed inflated value which they conceded no investor may properly claim) (App. Br. 18 n.9); and the very premise of the fraud-on-the-market theory on which modern securities litigation is largely based is that upon earlier public disclosure the price would have dropped in the same manner that it did when USSC made its April 7 announcement. It would therefore be purely undisciplined speculation to conclude that petitioners, or any other investor, could get out faster than the analysts, market professionals, or others as the market promptly absorbed the bad news. A jury would have no means but guesswork or prejudice to make such assessments.[11] And

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[10](...continued)

> vexatious litigation over "many rather hazy issues of historical fact the proof of which depended almost entirely on oral testimony." [*Blue Chip Stamps*, 421 U.S.] at 743.

[11] As the Fifth Circuit saw in similar circumstances,

> The flaw in the [plaintiffs'] argument is that . . . had this information been released, the stock price would have immediately and precipitously fallen especially if, as is implicit in the Crockers' theory, an entire class of shareholders had simultaneously dumped their stock on the market. Thus, there would have been no market for the stock at the artificially high price. Without such a market, the [plaintiffs'] envisioned "profit opportunity" evaporates into hardly more than an illusion.

Crocker v. FDIC, 826 F.2d at 351-52.

the wrong cannot be viewed as the failure to say "no comment" (leaving Chanoff no better off than shareholders generally), as doing so causes an insuperable proximate cause problem: the failure to say "no comment" was clearly not the proximate cause of petitioners' losses.[12]

III. THE *BLUE CHIP STAMPS* ISSUE IS NOT PROPERLY PRESENTED, AS DISMISSAL OF THE RICO CLAIMS WAS CORRECT ON GROUNDS NOT WARRANTING REVIEW

Dismissal of the RICO claims rested on multiple grounds, and this case is no better vehicle than was *Holmes v. Securities Investors Protection Corp.* for deciding whether the *Blue Chip Stamps* rule generally applies to RICO cases based on predicate acts of securities fraud.

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[12] Petitioners do not allege that they would have sold their shares had Scipione simply answered "no comment" and referred Chanoff to the public record. Far from alleging any fixed intention to sell that was undermined by the asserted personal misrepresentations, petitioners conceded that because of the appreciation of 400,000 shares acquired many years previously, Chanoff had developed the fixed intention to retain based on public disclosures. A260 ("Mr. Chanoff never had any intention of selling his U.S. Surgical stock. It was his intention to hold that stock for long-term appreciation and have it become part of his estate"). *Cf. Goldman v. Feinberg*, 37 A.2d 355, 356 (Conn. 1944) (to obtain tort damages for lost profits, plaintiff must "show that he was not only 'about to,' but would, but for the malicious interference of the defendants, have entered into the contract . . .").

Of course, petitioners cannot eliminate uncertainty from their damage calculations by contending that the wrong was only the failure to provide information selectively to William Chanoff, rather than the failure to provide that information to the market generally, since doing so would have violated compelling and controlling federal norms against such conduct.

First, the remaining RICO claims were properly dismissed because petitioners failed to allege any injury to their "business or property" proximately caused by defendants' conduct, as required by 18 U.S.C. § 1964(c) (1984). They lost no shares, their ability to sell their shares was never impaired, and they lost no money to which they were entitled (*see* n. 8 *supra*), having neither bought at an artificially inflated price nor sold at an improperly deflated price. In this context, hypothetical lost profits are not a cognizable property interest for purposes of defining a RICO wire or mail fraud predicate felony. *United States v. Miller*, 997 F.2d 1010 (2d Cir. 1993).

Second, following the approach of *Holmes v. Securities Investors Protection Corp.*, 112 S. Ct. 1311 (1992), which avoided the purchaser-seller issue by analyzing plaintiffs' claims under traditional proximate cause principles, the district court held that plaintiffs failed to allege any non-speculative damages that could be found proximately caused by the alleged RICO violation. Pet. C-22-24; *see also, e.g., Lewis v. Robinson*, No. 94-7131, 1994 U.S. App. LEXIS 30514 (2d Cir. Nov. 1, 1994) (affirming dismissal for lack of proximate causation); *Commercial Union Assurance Co. Plc v. Milken*, 17 F.3d 608 (2d Cir. 1994) (case dismissed on summary judgment, as plaintiffs could not show compensatory damage); *Hecht v. Commerce Clearing House, Inc.*, 897 F.2d 21, 22 (2d Cir. 1990) (Rule 12(b)(6) dismissal where damages not proximately caused by alleged RICO violation); *Barrows v. Forest Labs., Inc.*, 742 F.2d 54, 60 (2d Cir. 1984) (dismissing securities fraud claims based on speculativeness of damages).[13]

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[13] *See also Fleischhauer v. Feltner*, 879 F.2d 1290, 1300 (6th Cir. 1989), *cert. denied*, 494 U.S. 1027 (1990) ("[t]he conduct of the defendants . . . caused the parties to invest in the films but it did

(continued...)

Third, at least for cases such as this, the plain statutory language of RICO compels a transactional connection between the alleged fraud and a sale of securities. Where securities fraud is alleged as a predicate act, "The statute unmistakably requires that there be fraud, sufficiently willful to constitute a criminal violation, *and that there be a sale of securities.*" *See Holmes*, 112 S. Ct. at 1325 (O'Connor, J., concurring) (emphasis added); *see also Blue Chip Stamps*, 421 U.S. at 731-36 (*Birnbaum v. Newport Steel Corp.*, 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S.956 (1952) purchaser-seller limitation is supported by statutory language of § 10(b), 15 U.S.C. § 78j(b) (1994), prohibiting fraud only "in connection with the purchase or sale of any security" and not otherwise). In *Holmes*, although the SIPC, as a stand-in for the insolvent securities firm, had not actually been the purchaser, the insolvent firm was clearly injured by fraud *in the sale of securities*. Here, by contrast, not only did petitioners not sell their securities, but also they were not harmed by alleged fraud in the sale of securities.[14]

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[13](...continued)
not cause the investment items to become less profitable than defendants represented . . ."); *In re American Express Co. Shareholder Litig.*, 840 F. Supp. 260 (S.D.N.Y. 1993) (an employee's loss of commissions may have been factually, but were not proximately, caused by defendants' RICO violations), *aff'd sub nom. Lewis v. Robinson*, No. 94-7131, 1994 U.S. App. LEXIS 30514, at *23-24 (2d Cir. Nov. 1, 1994).

[14] Justice O'Connor's concurring opinion in *Holmes* addressed the somewhat different question concerning standing. The standing issue in *Holmes* was whether the SIPC, which had never held or traded the relevant shares but was suing under a subrogation theory, could sue under § 1964(c), which limits standing to "any person injured in his business or property." The "plain statutory language" reasons Justice O'Connor gave for not superimposing the
(continued...)

Nor can petitioners rely on the respondents' alleged sales of their own USSC stock into the market to establish the necessary predicate acts of "fraud in the sale of securities." Petitioners have not been "injured in [their] business or property by reason of" respondents' alleged predicate acts of "fraud in the sale of securities,"[15] as petitioners did not trade contemporaneously with any of the defendants. *See* Pet. C-16 n.10.

Even if the RICO claims had been dismissed under the sole authority of *Blue Chip Stamps*, review would not be warranted, as the *Blue Chip Stamps* rule should be applied in cases like this, either to require that plaintiffs have purchased

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[14](...continued)

Blue Chip Stamps purchaser or seller limitation onto the standing requirement of § 1964(c) are inapposite here, where the question is not one of standing but rather whether petitioners have alleged racketeering activity concerning "fraud in the sale of securities" under the § 1961(1) definition of "racketeering activity." Any injury petitioners here can complain of is not caused, as it was in *Holmes*, by fraud "in the sale of securities." *See* 112 S. Ct. at 1315.

Justice O'Connor went on to consider another question not presented here, whether a "purchaser/seller" standing limitation could be justified under the definition of "racketeering activity" in § 1961(1), and concluded that "the predicate offense does not *necessarily* dictate that a RICO plaintiff have been a party to an executed sale." 112 S. Ct. at 1325 (emphasis in original). But the concurrence does not suggest that a RICO claim may be pleaded where, as here, plaintiffs are neither parties to a sale nor have themselves been harmed by fraud in the sale of securities. To the contrary, Justice O'Connor's analysis expressly required a sale as an element of the statute.

[15] *See also Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 497 (1985); *American Nat'l Bank & Trust Co. v. Haroco, Inc.*, 473 U.S. 606, 609 (1985); *Fleischhauer v. Feltner*, 879 F.2d at 1300.

or sold, or at least to the extent of requiring that plaintiffs have been injured by fraud in the sale of securities. *See International Data Bank, Ltd. v. Zepkin*, 812 F.2d 149, 152-53 (4th Cir. 1987) (RICO plaintiff relying on securities fraud as predicate offense must have been purchaser or seller); *Brannan v. Eisenstein*, 804 F.2d 1041, 1046 (8th Cir. 1986) (same).[16]

Setting RICO claims based on securities fraud allegations adrift from *Blue Chip Stamps* would be tantamount to jettisoning that case altogether. Because virtually every Rule 10b-5 lawsuit arising from misrepresentations and omissions

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[16] *See also Powers v. British Vita P.L.C.*, 842 F. Supp. 1573, 1583 (S.D.N.Y. 1994) (non-purchaser of securities did not have standing to advance a Rule 10b-5 securities fraud claim under RICO); *Viacom Int'l Inc. v. Icahn*, 747 F. Supp. 205, 210 (S.D.N.Y. 1990), *aff'd*, 946 F.2d 998 (2d Cir. 1991), *cert. denied*, 112 S. Ct. 1244 (1992) ("[p]laintiff must have been directly involved in either the purchase or sale of the securities in the Rule 10b-5 allegations to have standing under RICO to assert a Rule 10b-5 violation as a predicate act of racketeering . . ."); *In re Par Pharmaceutical, Inc. Secs. Litig.*, 733 F. Supp. 668, 684 (S.D.N.Y. 1990) ("[F]raud in the Sale of Securities" as used in RICO § 1961(1)(D) applies only if fraud occurred in the actual sale, as opposed to the purchase, of securities); *Beres v. Thomson McKinnon Secs., Inc.*, [1990-91 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,722, at 98,402 (S.D.N.Y. Dec. 20, 1990) (court dismissed plaintiff's RICO securities fraud claim because the plaintiff neither purchased nor sold securities); *Chief Consol. Mining Co. v. Sunshine Mining Co.*, 725 F. Supp. 1191, 1194 (D. Utah 1989) ("private persons have standing to bring RICO claims based on securities violations under Rule 10b-5 only if they are purchasers or sellers of securities . . ."); *Kravetz v. Brukenfeld*, 591 F. Supp. 1383, 1390 (S.D.N.Y. 1984) (a RICO securities fraud claim predicated on a Rule 10b-5 violation requires fraud in the sale of securities). *Contra, Pelletier v. Zweifel*, 921 F.2d 1465, 1510-11 n.80 (11th Cir.), *cert. denied*, 112 S. Ct. 167 (1991); *Warner v. Alexander Grant & Co.*, 828 F.2d 1528, 1530 (11th Cir. 1987).

can be augmented with RICO claims based on the same facts, accepting petitioners' argument would, to paraphrase *Ultramares Corp. v. Touche*, 255 N.Y. 170, 186-87 (1931), render the carefully considered holding in *Blue Chip Stamps* nothing but a

> snare, entrapping litigants and lawyers into an abandonment of the true remedy lying ready to the call. The suitors thrown out of court because they proved [securities fraud], and nothing else, in an action [under Rule 10b-5], might have ridden to triumphant victory if they had proved the self-same facts, but had given the wrong another label [RICO] . . . .

It would be illogical in the extreme to find the dangers identified by this Court in *Blue Chip Stamps* and *Virginia Bankshares* so substantial that mere holders may not bring suits for even actual damages, while at the same time totally to disregard those same dangers (and indeed augment them) in cases based on the same facts by exposing those same defendants and courts to RICO suits for *treble* damages. Such a result should not be adopted unless RICO's statutory language leaves no alternative. *Cf. Virginia Bankshares*, 501 U.S. at 1106 ("[g]iven a choice we would reject any theory . . . that raised such prospects [those identified in *Blue Chip Stamps*], and we reject this one . . .").

In light of the statutory reference in 18 U.S.C. § 1964(c) to fraud "in the sale of securities," and legislative history making plain that the "evil" at which 18 U.S.C. § 1964(c) was aimed was not assertions of inaccuracy in routine corporate disclosures but rather so-called "boiler-room broker-dealer operation"[17] and efforts by organized crime

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[17] The "boiler-room broker-dealer operation," which first drew attention in the late 1960's, refers to high-pressure operations (continued...)

illegally to gain control of brokerage firms and then use that position either to sell fraudulent stock or manipulate prices by purchasing controlling interests in closely held corporations,[18] there is compelling reason not to read RICO as eviscerating the salutary policies of *Blue Chip Stamps*.

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[17](...continued)
selling highly speculative or worthless securities of issuers without substantial businesses, *see, e.g., Hanly v. SEC*, 415 F.2d 589, 597 (2d Cir. 1969); *United States v. Goldberg*, 401 F.2d 644, 647 (2d Cir. 1968), *cert. denied*, 393 U.S. 1099 (1969), and to the theft of securities and their later resale by organized crime, often resulting from pressure on back-room employees of brokerage houses and other institutions in the Wall Street area to repay loans made to them by organized crime or to repay gambling debts. *See The Federal Effort Against Organized Crime: Hearings Before a Subcommittee of the House Committee on Government Operations*, 90th Cong., 2d Sess. 325 (1968) (hereafter "*Federal Effort Hearings*") (statement of Irving M. Pollack, Director, Division of Trading and Markets, SEC); 115 Cong. Rec. 7607-08 (1969)(article by Patrick Young, included in statement of Rep. John M. Murphy).

[18] *See Federal Effort Hearings*, at 455; 113 Cong. Rec. 17,998 (1967) (statement of Sen. Hruska).

CONCLUSION

For all the foregoing reasons, the petition for a writ of *certiorari* should be denied.

New York, New York
November 18, 1994

Respectfully submitted,

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